

GENERAL INFORMATION

The Community Reinvestment Act (" CRA ") requires each federal financial supervisory agency to use its authority when examining financial institutions subject to its supervision to assess the institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of the institution. Upon conclusion of such examination, the agency must prepare a written evaluation of the institution's record of meeting the credit needs of its community.

This document is an evaluation of the CRA performance of Farmers State Bank, Faith, South Dakota, prepared by the Federal Reserve Bank of Minneapolis, the institution's supervisory agency, as of July 21, 1997. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 CFR Part 228.

INSTITUTION'S CRA RATING: This institution is rated "Satisfactory."

There are a number of factors that support the bank's satisfactory rating. First, the bank provides most of its consumer loans to low- and moderate-income borrowers. In addition, the bank has a reasonable distribution of loans to businesses and farms of different sizes. Second, the bank has a reasonable distribution of loans among geographies of different income levels. Third, the bank maintains a high loan-to-deposit ratio. Finally, the bank has made a significant number of its loans within its assessment area.

DESCRIPTION OF INSTITUTION

The bank is able to meet the credit needs of residents of its assessment area effectively. The bank received a satisfactory rating at its last CRA evaluation. The bank operates one full-service office in Faith, South Dakota. The office is centrally located in the bank's assessment area.

According to the June 30, 1997, Report of Condition ("ROC"), the bank has total assets of approximately \$25.5 million. According to quarterly ROC data, the bank's net loans have been increasing since December 1996. The bank's net loans have increased from \$14.7 million to \$17.5 million during that period. During the same period, deposits have declined from \$21.6 million to \$18.7 million. Poor agricultural conditions caused by severe weather last year resulted in a higher than usual number of carryover loans that normally would have been paid off with seasonal profits by year-end. The "carryover" loans have contributed to the increase in the bank's loan-to-deposit ratio since December 1996. The bank is primarily an agricultural lender. According to the June 30, 1997, ROC, approximately 84% of the bank's loan portfolio is agricultural and agricultural real estate loans. Consumer and commercial loans make up about 7% and 6% of the bank's loan portfolio, respectively. The remaining 3% of the portfolio contains residential real estate loans.

The bank offers a variety of loan products that help meet the credit needs of residents and businesses of its assessment area. It extends agricultural, commercial, and consumer loans. The bank offers Small Business Administration- and Farm Service Agency-guaranteed loans for commercial and agricultural borrowers. It also participates in the Dakota MAC program. This program allows lenders to offer loans secured by agricultural real estate for a variety of term lengths. The bank annually offers a Christmas loan program for consumers. Under this program, borrowers receive interest-free funds that can be used at participating Faith businesses during the holiday season. The loans may have maturities of up to nine months. Although the bank does not issue credit cards, it does refer credit card applicants to another financial institution. The bank at times sends a written referral for the applicant that discusses the applicant's creditworthiness for the loan.

DESCRIPTION OF FARMERS STATE BANK'S ASSESSMENT AREA

The bank's assessment area includes all or portions of four South Dakota counties: Meade, Perkins, Dewey, and Ziebach. The assessment area is located in north-central South Dakota, is very sparsely populated, and covers a relatively large geographical area. Only 14,279 residents live in the assessment area, based on 1990 census data. Meade County census tract 201 is included in the assessment area. Perkins, Dewey, and Ziebach counties are block numbering areas ("BNA") 9983, 9881, and 9871, respectively, and are all included in the assessment area. Ziebach and Dewey counties are part of the Cheyenne River Indian Reservation ("Reservation"). The bank's office is located in Meade County approximately 1 mile west of the Reservation's western boundary. Faith is approximately 130 miles northeast of Rapid City, South Dakota, and is a rural community with approximately 571 residents. The assessment area includes several small communities, such as Lemmon, Bison, Isabel, Timber Lake, Dupree, and Eagle Butte, South Dakota. The headquarters for the Cheyenne River Sioux Tribe ("Tribe") is located in Eagle Butte, a community approximately 50 miles east of Faith. A \$20-million bank operates in Eagle Butte.

CRA divides income levels into four categories: low, moderate, middle, and upper. Because the bank's assessment area is not in a metropolitan statistical area, the categorization of a borrower, census tract, or BNA is determined relative to the statewide nonmetropolitan median family income. Low-income individuals have incomes of less than 50% of the statewide nonmetropolitan median family income, while moderate-income individuals have incomes of at least 50% but less than 80% of this amount. Middle-income individuals have incomes at least 80% but less than 120% of the statewide nonmetropolitan median family income, and individuals with incomes of 120% or more of this amount are defined as upper income. According to 1990 census data, the statewide nonmetropolitan median family income is \$25,547. This figure is used to determine a geography's income level. The Department of Housing and Urban Development-adjusted statewide nonmetropolitan median family income for 1997 is \$34,500. This figure is used to determine a borrower's income level. According to 1990 census data, the median family income for the bank's assessment area is \$20,154, which is notably less than South Dakota's average nonmetropolitan median family income.

Of the four geographies in the bank's assessment area, census tract 201 and BNA 9983 are middle-income geographies, and BNAs 9871 and 9881 are moderate-income geographies. Approximately 7,743 residents, or 54% of the assessment area's population, live in the assessment area's moderate-income BNAs. The remaining 6,536 residents, or 46% of the assessment area's population, live in the middle-income census tract and BNA.

The assessment area has 4,830 households and 3,617 families. Approximately 31% of the assessment area's households are low income, 17% are moderate income, 18% are middle income, and 33% are upper income. Low-income families represent about 33% of the assessment area's total families. Moderate-income families make up another 17% of the assessment area's families, whereas middle- and upper-income families represent about 21% and 29% of the assessment area's families, respectively. The assessment area also has a large number of elderly residents. Bank management estimates that as many as 40% of the area's residents are elderly. Normally, elderly residents have little demand for credit.

The assessment area contains 1,398 households with incomes below the poverty level, which represent about 29% of the assessment area's total households. Based on family information, the assessment area has 1,026 families with incomes below the poverty level, or about 28% of total families. Both the assessment area's household and family poverty figures significantly exceed the statewide nonmetropolitan household and family poverty figures of 18% and 14%, respectively. Ziebach and Dewey counties have significantly higher levels of households and families with incomes below the poverty level than do Meade and Perkins counties. In Dewey County, approximately 39% of the households and 40% of the families have incomes below the poverty level. In Ziebach County, about 44% of the households and 43% of the families have incomes below the poverty level.

Examiners made community contacts with individuals familiar with the conditions in the assessment area, including several tribal members and a Faith resident. Information from these contacts as well as information from bank management was used in evaluating the bank's CRA performance. According to the contacts, the economic condition of the assessment area is poor. Unemployment on the Reservation is high; one contact said it may be as high as 80%. In addition, tribal contacts indicated that few tribal members have the capital needed to begin a ranching operation on their allocated tribal trust land. As a result, many members lease this land to nontribal members. While one contact indicated that unemployment may not be a problem in the nonreservation portions of the assessment area, the contact indicated wages are low and many young people leave the community after graduating from high school to

seek better wage opportunities. Census data from 1990 indicate that approximately 8% of the assessment area's residents are unemployed.

Although Faith has several small businesses, it has virtually no industry. Its major employers include a livestock sale operation, the local school, and city government. One contact believes Faith's distance from major transportation networks limits the chance of much industrial growth in the area. Tribal contacts indicated that its employed members primarily have tribal government positions. They added that the Reservation has few individually owned businesses.

All contacts indicated that affordable housing is needed in the assessment area. According to the tribal contacts, the tribal government provides housing for most tribal members. Unfortunately, housing conditions have deteriorated because individuals lack repayment sources to qualify for home improvement loans from the Tribe. In the assessment area's nonreservation sections, one contact indicated that housing values are so low that there is little incentive to improve or build new units. As a result, many homes in the Faith area are rather dilapidated. Many residents purchase mobile homes rather than purchase homes. Bank management indicated that there is little demand for housing loans in the area. Based on 1990 census data, the median housing value in the assessment area is very low at \$25,255, which is less than the statewide nonmetropolitan median housing value of \$37,142.

Bank management and community contacts stated that the assessment area's economy is driven by agriculture. The main agricultural commodities in the area include cattle, sheep, and winter wheat. Low cattle prices in recent years have hurt the area's agricultural economy. As discussed previously, current agricultural conditions have also suffered because of the severity of the recent winter. According to bank management, these conditions have led to a strong demand for agricultural loans, primarily for the extension of existing loans.

The assessment area contains several competitor banks. As discussed, a small bank operates in Eagle Butte. Other banks operate offices in Dupree, Timber Lake, and Isabel. Lemon and Bison contain branches of a relatively large bank based in Aberdeen, South Dakota. Because of the distance between Lemmon and Faith, the bank serves few customers in the northern section of Perkins County (BNA 9983).

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

The bank has done a satisfactory job of meeting the credit needs of its assessment area. Much of the analysis on the following pages was based on a statistical sample of 81 agricultural, 123 consumer, and 42 commercial loans originated since the last evaluation. In the discussion that follows, the income and geographic distribution sections are given the most weight in supporting the bank's satisfactory rating.

LOAN-TO-DEPOSIT RATIO ANALYSIS

The bank's loan-to-deposit ratio exceeds the standards for satisfactory performance based on its consistently high level, its comparison to local competitors, and the demand for loans in the assessment area. Since the previous evaluation, the quarterly average of the bank's net loan-to-deposit ratio is 78.6%. According to the June 30, 1997, ROC, the bank's loan-to-deposit ratio was 93.7%. The following chart shows the bank's lending and deposit activity since June 30, 1997.

Date	Net Loans (In thousands)	Deposits (In thousands)	Net Loan-to-Deposit Ratio
June 30, 1996	\$15,010	\$19,169	78.3%
September 30, 1996	\$14,705	\$21,210	69.3%
December 31, 1996	\$14,741	\$21,640	68.1%
March 31, 1997	\$16,182	\$19,346	83.6%
June 30, 1997	\$17,549	\$18,725	93.7%

As shown above, the bank's lending levels have increased since the last evaluation. The chart above reflects the increase in agricultural loans resulting from the carryover debt situation discussed previously. Bank management also attributed some of the increase in loans to the bank's active installment loan program.

As discussed in the Description of the Assessment Area section, the bank has several competitors in the assessment area. The chart below details the competitors' asset sizes and average loan-to-deposit ratios since March 31, 1996.

Bank Name	Total Assets March 31, 1997 (In thousands)	Quarterly Average Net Loan-to-Deposit Ratio
First Financial Bank South Dakota Dupree, South Dakota	\$52,619	62.8%
State Bank of Eagle Butte Eagle Butte, South Dakota	\$19,850	50.2%
Western Dakota Bank Timber Lake, South Dakota	\$11,563	49.2%

The bank's quarterly average net loan-to-deposit ratio since March 31, 1996, is 74.8%. As such, the bank's average net loan-to-deposit ratio is significantly higher than that of its competitors.

According to Uniform Bank Performance Report ("UBPR") data, the bank's net loan-to-deposit ratio was 83.6% as of March 31, 1997. The peer average for the same date was 59.9%. The bank's ratio places it in the 95th percentile compared with its peers. The bank's loan-to-deposit ratio substantially exceeds the ratios of its competitors and most of its national peers. In addition, the bank's ratio indicates that it is an active lender; community contacts did not indicate any unmet credit needs in the assessment area. Given these factors, the bank's loan-to-deposit ratio exceeds the standards of satisfactory performance.

COMPARISON OF CREDIT EXTENDED INSIDE AND OUTSIDE THE ASSESSMENT AREA

The bank's performance in lending within its assessment area exceeds the standards for satisfactory performance. Examiners reviewed a sample of bank loans to determine the percentage of loans made in the assessment area. The results of the loan sample showed that the bank makes the vast majority of its loans in its assessment area. The following table shows the percentage of loans by total number and total dollar amount made in the assessment area.

PERCENTAGE OF LOANS IN THE ASSESSMENT AREA		
Loan Type	Total Number of Loans	Total Amount of Loans
Consumer	92	92
Agricultural	91	82
Commercial	86	77

As discussed previously in the Description of the Assessment Area section, the bank has few opportunities to provide business loans in its assessment area. The bank made only 43 commercial loans since the previous evaluation. Of these loans, the bank made six to commercial borrowers located just outside the assessment area. In its primary lending category, agricultural loans, the bank made more than 90% of its loans in its assessment area. The percentages of bank loans made in the assessment area indicate the bank is lending to individuals, businesses, and farms in its assessment area. Because the bank made the vast majority of its loans in its assessment area, its lending activity in this category exceeds the standards for satisfactory performance.

LENDING TO BORROWERS OF DIFFERENT INCOME LEVELS AND TO BUSINESSES OF DIFFERENT SIZES

The bank's lending to borrowers of different income levels and businesses of different sizes exceeds the standards for satisfactory performance. As discussed previously, CRA divides borrowers into four income categories: low, moderate, middle, and upper. Although consumer loans constitute a relatively small percentage of the bank's loan portfolio, the bank provides a significant number of such loans. The loans do not represent a significant portion of the loan portfolio because many have very small dollar amounts. As the following chart shows, the bank's lending to individuals with low and moderate incomes is impressive.

DISTRIBUTION OF LOANS BY INCOME LEVEL IN THE ASSESSMENT AREA*				
Loan Type	Low Income	Moderate Income	Middle Income	Upper Income
Consumer:				
Total Number of Loans	58%	36%	4%	2%
Total Amount of Loans	34%	55%	5%	6%
*Income level is determined based on South Dakota's 1997 nonmetropolitan median family income of \$34,500.				

As shown above, the bank made almost all of its consumer loans to low- and moderate-income individuals. This level of lending to low- and moderate-income individuals is particularly commendable given that only about 49% of the assessment area's households are considered low and moderate income. Moreover, a substantial portion of these residents have incomes below the poverty level. Several reasons explain why the bank makes few consumer loans to middle- and upper-income borrowers. First, as shown in the chart, a borrower's income level is determined based on a statewide average median family income of \$34,500. It is likely that the assessment area's median family income is lower than this figure. Based on 1990 census data, the assessment area's median family income was about \$5,000 less than the statewide nonmetropolitan median family income. This difference suggests that incomes are generally lower in the assessment area than in other parts of the state. As such, more assessment area borrowers would be

classified low and moderate income when compared with a statewide average income figure than would be classified in higher-income nonmetropolitan areas. Second, bank management said the bank makes a concerted effort to provide small dollar amount loans to low- and moderate-income individuals. Third, the bank did not have income information for approximately 28% of the consumer loans sampled. Bank management indicated that it collects income information mostly for new borrowers. As such, it is possible that some of the bank's regular customers have higher incomes and the incomes of these customers did not get included in the sample. Nevertheless, of the more than 80 loans with income information, the bank made almost all of these loans to low- and moderate-income borrowers.

Primary emphasis is placed on the bank's loans to small farms given that the bank is primarily an agricultural lender. The bank made all the sampled agricultural loans to farms with less than \$1 million in gross annual revenues. Further analysis of the bank's loans to small farms indicates that 86% of the total number and 39% of the total dollar amount of these loans involved loans for \$100,000 or less. An additional 11% of small farm loans involved loans of more than \$100,000 but less than or equal to \$250,000. The remaining 3% of loans were for amounts of more than \$250,000 but equal to or less than \$1 million.

The bank also made all the sampled commercial loans to businesses with less than \$1 million in gross annual revenues. The analysis of the bank's small business loans indicates that 97% of the total number and 79% of the total dollar amount of loans involved loans of \$100,000 or less. The remaining 3% of total loans were for amounts greater than \$100,000 but less than or equal to \$250,000. The bank's level of lending to small farms and businesses is expected given that the assessment area has few large businesses.

As discussed in the Description of the Assessment Area section, there is little demand for housing loans in the assessment area. The low level of housing values makes most residential real estate loans not attractive to most borrowers. Despite this lack of demand, bank management indicated that it will make residential real estate loans when possible. Although there is little demand for residential real estate loans, assessment area residents have a greater need for small consumer loans. A review of the bank's consumer loan sample shows that the bank makes many short-term, small dollar amount loans designed to serve the needs of mostly low- and moderate-income borrowers.

Even though the bank's small farm and small business lending reflects the nature of the assessment area, the bank's lending to low- and moderate-income borrowers and its willingness to make small dollar amount loans support the conclusion that the bank's lending to borrowers of different income levels and businesses of different sizes exceeds the standards for satisfactory performance.

GEOGRAPHIC DISTRIBUTION OF LOANS

The bank's performance in lending to individuals, farms, and businesses in geographies of different income levels meets satisfactory standards. As discussed previously, the assessment area includes two moderate-income and two middle-income geographies. The total population of the assessment area is 14,279; 54% of these residents live in moderate-income BNAs, and 46% live in the middle-income census tract and BNA. The following chart shows the distribution of loans by type and geography income level.

DISTRIBUTION OF LOANS BY CENSUS TRACT OR BNA INCOME LEVEL*		
Loan Type	Moderate-Income BNAs	Middle-Income Census Tract or BNA
Consumer		
Total Number of Loans	80%	20%
Total Amount of Loans	63%	37%
Agricultural		
Total Number of Loans	43%	57%
Total Amount of Loans	59%	41%
Commercial		
Total Number of Loans	25%	75%
Total Amount of Loans	30%	70%
*The assessment area does not have any low- or upper-income BNAs or census tracts.		

As shown in the above chart, the bank made 80% of the sampled consumer loans in the assessment area's moderate-income BNAs. As discussed previously, this area is part of the Reservation. The bank made fewer agricultural loans in the moderate-income BNAs. Specifically, the bank made 43% of the total agricultural loans in these BNAs. The bank's consumer and agricultural lending figures compare favorably with the percentage of assessment area residents residing in the moderate-income BNAs (54%). The bank made only 25% of its commercial loans in the assessment area's moderate-income BNAs.

The distribution of the bank's loans among the assessment area's moderate- and middle-income geographies accurately reflects loan demand patterns. As discussed previously, many Reservation residents are unemployed. As such, it seems plausible that few residents would qualify for most agricultural and commercial loans. In fact, tribal contacts indicated that most tribal members lack the capital needed to begin an agricultural operation. However, as shown by the distribution of the bank's consumer loans, many qualify for the bank's small dollar amount consumer loans. Tribal contacts also stated that the Reservation contains few individually owned businesses. The lack of Reservation businesses helps explain why the bank made the majority of its commercial loans outside the Reservation in the assessment area's middle-income geographies. Most of the assessment area's businesses are in Faith and Lemmon, communities located in a middle-income census tract and a middle-income BNA, respectively. Given that Faith is a significant distance from Lemmon, the bank makes few commercial loans in the Lemmon area.

A tract-by-tract analysis of the bank's lending patterns supports the previous discussion and shows a reasonable distribution of loans. The bank made most of its commercial loans in census tract 201, the tract that encompasses the city of Faith. Few business loan opportunities exist outside this tract within a reasonable distance of the bank. The bank made the majority of its agricultural loans in census tract 201 and BNA 9871. Both these geographies are close to the bank and contain the least number of competitor bank locations. The bank made few consumer loans in BNA 9983. This BNA is sparsely populated except for the community of Lemmon, which is more than 60 miles from the bank. Not only does this community have a relatively strong local bank, but it is a great distance from the bank, particularly for consumer loan customers.

In general, the bank's distribution of loans by geography income level and individual geography is reasonable given the assessment area's demographic, economic, and loan demand issues. As such, the bank's distribution of loans among geographies of different income levels meets the standards for satisfactory performance.

GENERAL

The evaluation did not reveal any violations of the substantive provisions of the fair lending and fair housing laws and regulations. The evaluation did reveal, however, a violation of the technical provisions of Regulation B--Equal Credit Opportunity Act. The bank has not received any CRA-related complaints since the last CRA evaluation.

PUBLIC DISCLOSURE

July 21, 1997
Date of Evaluation

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

Farmers State Bank
Name of Depository Institution

094605200000
Identification Number of Institution

Faith, South Dakota
Address of Institution

Federal Reserve Bank of Minneapolis
90 Hennepin Avenue
Minneapolis, Minnesota 55480-0291

NOTE: This evaluation is not, nor should it be construed as, an assessment of the financial condition of this institution. The rating assigned to this institution does not represent an analysis, conclusion, or opinion of the federal financial supervisory agency concerning the safety and soundness of this financial institution.